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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1955

No. 134

CLARK SQUIRE, Collector of Internal Revenue for the District of Washington,

Petitioner,

vs.

HORTON CAPOEMAN and EMMA CAPOEMAN, His Wife

BRIEF FOR RESPONDENTS

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BRIEF FOR RESPONDENTS

Questions Presented

1. Is allotted land on the Quinaielt Indian Reservation which was never transferred free of restriction to the Indian allottee, subject to capital-gains tax upon its conversion by the United States into cash, notwithstanding the trust assumed by the United States to transfer the land to him "free of all charge or incumbrance whatsoever"?

2. Is there a "basis" for capital gain tax on the sale of timber growing on restricted, allotted Indian land held by the United States in trust and never, prior to the sale of the timber, transferred to the allottee, outright in accordance with the Congressional scheme, which basis is other or dif-

ferent than the proceeds realized by the United States to be held for the allottee?[1]

Statement

When white men came to the Olympic Peninsula, they found the Quinaielt Tribe and their neighbors, the Quillieute, occupying a tract of country lying between the Coast Range and the Pacific ocean. This land (save for the reservation of certain lands for their exclusive use, Art. II), the Quinaielts and Quillicutes ceded just a century ago to the United States by Treaty of July 1, 1855, and January 25, 1856, 12 Stat. 971, Art. I. It is on the reservation set up pursuant to this treaty that respondents, fullblood Quinaielt Indians, live. R. 33, 34-35.

In the treaty it had been understood that the Quinaielts should have exclusive use of their reservation "and no white man shall be permitted to reside theron without permission of the tribe" (Art. II). But a new approach to the "Indian problem" resulted in the enactment of the General Allotment Act of 1887, c. 119, 24 Stat. 388, 25 U.S.C. § 331, *et seq.* Thereunder, Indians were to be allotted lands on their reservations not to exceed 160 acres of grazing land or 80 acres of agricultural land; and 25 years after allotment the allottees were to receive the lands discharged of the trust under which the United States had theretofore held them and to take a patent "in fee discharged of said trust and free of all charge or incum-

[1] The question of there being no capital asset, hence no basis, until the land (or the proceeds of its conversion) be transferred to the allottee free of all charge or incumbrance whatsoever was a ground of the decision of the District Court (R. 56-57). It was not expressly adverted to by the Court of Appeals. Even were it ruled against respondent in the Court of Appeals it would be open upon review of the merits in this Court, since its resolution in accordance with respondents' theory would support the judgment of the court below. *Langnes* v. *Green*, 282 U.S. 531, 538-9.

brance whatsoever" (25 U.S.C. § 348), though the President might extend the period.

Under the General Allotment Act of 1887 petitioner was allotted from the treaty-guaranteed reservation 93.35 acres and received a trust patent October 1, 1907 (R. 13, 35). The patent represents (R. 14) that the United States

> "does and will hold the land thus allotted (subject to all statutory provisions and restrictions) for the period of twenty-five years, in trust for the sole use and benefit of the said Indian, and that at the expiration of said period the United States will convey the same by patent to said Indian, in fee, discharged of said trust and free of all charge or incumbrance whatsoever, if the said Indian does not die before the expiration of the trust period; but in the event said Indian does die before the expiration of that period this patent and the allotment upon which it is based shall be canceled, and the said land shall revert to the United States and be thereafter disposed of in the manner prescribed by law."

The title continues to be held in trust (R. 35).

In 1943 standing timber on respondent Indian's allotment was cut, sold and paid for pursuant to a contract by the Bureau of Indian Affairs with the approval of respondents, the sales price being the amount of $8,418.28 (R. 36). From this, $2,026.80—being the fair market value of the timber March 31, 1913, as determined by the forest ranger at Taholah Indian Agency (R. 20)—was deducted, together with $673.46 expenses of sale (R. 18), leaving a "gain" of $5,718.64, of which 50%, or $2,859.32, was taken into account (R. 18, 15-16) as a long-term capital gain in computing respondents' income tax for 1943. The tax computed on this theory was paid from the trust fund proceeds in the hands of the Indian agency (R. 19-20) and respondent

sued upon denial (R. 28) of a timely claim for refund (R. 20-22).

Judge Fee held (R. 55-57) respondents entitled to recover. The United States having taken this property with the obligation to convey it at the end of the trust period to the allottee in fee "discharged of said trust and free of all charge or incumbrance whatsoever", it follows that until the allottee is put in possession of the land on those terms —namely, the whole corpus of the trust which it has been agreed will be turned over to him free of all charge or incumbrance—the land cannot be treated as an ordinary "capital asset" for tax purposes. He pointed out that immediately on turning over to an Indian a patent in fee, the Indian receives a value greater than the March 1, 1913, value or the value on the date of the treaty; but if, thereupon, the Federal government taxed that increment, it would destroy the value of the trust property and violate its undertaking. Timber is a part of the land, and the proceeds of timber here are a substitute for the land itself. Merely by selling and cutting the timber, the trustee does not relieve itself of the trust, or become entitled to help itself to proceeds of that which it had promised to put in the hands of respondents.

The Court of Appeals for the Ninth Circuit (Healy, Bone and Chambers, JJ.) affirmed per curiam, noting general agreement with Judge Fee and noting also that "this attempt to tax evidences, at the least, a sorry breach of faith with the Indians." It found no ground for the distinction which Judge Fee had supposed of the decision of the Tenth Circuit in *Jones v. Tannah*, 186 F. 2d 445, but expressly agreed with the dissenting opinion of Chief Judge Phillips in that case (R. 58-59).

Summary of Argument

1. This case involves no question of the ordinary annual product, such as agricultural crops, of an Indian's land or labor, but the capital value itself of an allotment of tribal land. Congress has said that the allottee is ultimately to get that land "in fee, discharged of said trust and free of all charge or incumbrance whatsoever"; that only thereafter shall the land be subject to "sale, incumbrance, or taxation"; and that in no event shall the land become liable to the satisfaction of "any debt" (federal income taxes are debts) contracted prior to the patent in fee. The land thus to be received includes the timber. Diminution in value is "incumbrance" of the land: and for the government to help itself to the proceeds of the land (timber) is clearly "incumbrance".

Congress has deliberately adopted a policy of protection of the allotment during the apprenticeship of restricted, reservation Indians. To permit petitioner to take a substantial part of the capital value of the land under the guise of taxes is inconsistent with that plain policy of Congress to preserve it intact. It is conceded by petitioner that the Congressional policy flatly forbids real-estate taxes under state authority. Would the Congressional policy which strained at the gnat of the local real-estate tax readily swallow the cannonball of the federal income tax, where both are paid at the expense of the very property?

The only value of these lands is in the forest product; and the subversion of the Congressional policy that respondent should have the lands without diminution is glaring in the light of the value of the land with and without the forest on it. These restrictions on incumbrance, including dissipation of the land through taxes, are a prop-

erty right; the terms are part not merely of the statute but of the so-called "trust patent" issued pursuant to the statute. If they have been repealed *pro tanto* as to the federal income tax, that is so because the income-tax statutes are construed as an implied repeal. This will not be the construction because repeals by implication are not favored; repeal would raise a serious constitutional question of the taking of respondent's property right without just compensation; and there is no clear and manifest intention of the legislature to repeal since it has affirmatively recognized the need for continuance of the restrictions. The Congressional policy in the allotment acts is a political question, which petitioner should not ask this Court to revise. Here the government is sharing in the capital itself —an invasion of the trust *res* which merely masquerades as a tax.

2. Respondent husband was not engaged in the "cutting and sale of timber, an ordinary income-producing operation", as petitioner asserts. That is logging. No part of the proceeds of the timber represented the labor or enterprise of respondents; there was simple substitution of the cash asset for the timber, both held by the government. The only connection this allottee had with what was done with his timber was to consent to its sale. In that capital transaction, the sale, respondent allottee has not even yet "acquired" his land, or its substitute, the proceeds. Until he receives that capital without charge or incumbrance, he has never yet "acquired" the land so as to be subject at all to the capital-gain provision. The provisions permitting a taxpayer to elect to apply depletion principles to timber which he purchases are inapplicable because respondents did not engage in the logging business, those depletion provisions are no better designed than are the capital-gain provisions to carry out the Congressional purpose to place respondents in possession of the undiminished capital

value of their land, and in any event the capital-gains treatment constituted an election that is binding on petitioner as well as these respondents.

Petitioner's argument that "these Indians are not entitled to any better treatment than is accorded to other taxpayers who own timber lands and who are taxed with income as it is realized" bespeaks a prejudice on the so-called "Indian problem". That problem is far more complicated than the casual or uninformed person, who follows the same line of thought, might suppose. Though petitioner, and even this Court, might not agree with the Congressional policy of handling that problem, the Congressional policy with respect to these non-competent, full-blood, reservation Indians must control.

ARGUMENT

I. This Is Not a Question of Tax Exemption, But Whether a Specific Trust Assumed by the United States Shall Be Avoided by Cloaking Its Invasion as a "Tax".

We are not dealing here with the ordinary annual product, such as agricultural crops, of an Indian's land or labor. With respect, for instance, to the annual products of a restricted or trust allotment, a noncompetent Indian may be either taxable[2] or non-taxable,[3] a question which

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[2] Garry *v.* Commissioner Int. Rev. (1955), 24 T.C. No. 23 (rentals of restricted allotments).

Jones *v.* Taunah (C.A. 10, 1951), 186 F. 2d 445, cert. den. 341 U.S. 904, No. 568 O.T. 1950 (agricultural-lease income, all judges concurring; oil-royalty income, one judge dissenting).

[3] Nicodemus v. United States (D.C. Id., 1955), 132 F. Supp. 608 (proceeds of grain).

United States *v.* Homeratha (W.D. Okla., 1930), 40 F.2d 305, app. dis. 49 F.2d 1086 ("rents, profits and mineral, especially oil and gas").

Pitman *v.* Commissioner Int. Rev. (C.A. 10, 1933), 64 F.2d 740 (oil bonus and royalties as to "homestead" lands of a member of the Five Civilized Tribes).

need not be resolved here because not presented on this record, there being in this case no such annual income to be concerned with.[4]

Whatever might be the case with respect to annual income from a trust allotment, we are concerned here with the land itself. The land marked out to be allotted to respondent husband was never freed from the trust restrictions under which it was segregated from the tribal holdings. (R. 35.) He has never yet received the land in fee, without diminution or encumbrance. The stand of timber here involved could not be realized by the allottee as can annual products of the land. (R. 35-6, § VII) And yet the United States has said that he is first to get that land before he may encumber it in any way; that at the expiration of the trust period he shall have a patent to the land (25 U. S. C. § 348, Petr. Brf. p. 41)—

> "in fee, discharged of said trust and free of all charge or incumbrance whatsoever."

And the land thus to be received includes the timber; "The timber while standing is a part of the realty, and it can only be sold as the land could be. The land cannot be sold by the Indians; and consequently the timber, until rightfully severed, cannot be." *United States v. Cook*, 19 Wall. 591, 593. Cf. *Northern Pac. R. Co. v. Paine*, 119 U.S. 561, 564; *Starr v. Campbell*, 208 U.S. 527, 534. The

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[4] The two cases repetitively relied upon by petitioner are not even as nearly related to the present case as are those in notes 2 and 3. One (Choteau *v.* Burnet, 283 U.S. 691) involves a competent Indian, hence does not involve restricted or "trust patent" lands at all. The other (Superintendent Five Civ. Tr. *v.* Commissioner Int. Rev., 295 U.S. 418) involves ordinary investment income, the only connection with trust-patent land being that originally the source of the funds to be invested had been the product of the land.

statute expressly says that only *after* the patent in fee is issued will the land (timber) be subject to "sale, incumbrance, or taxation."[5] 25 U.S.C. § 349 (quoted Petr. Brf. p. 43). The statute says twice that allotted land "shall not be liable to the satisfaction of any debt contracted prior to the issuing of such patent" (25 U.S.C. § 349; quoted, Petr. Brf. p. 43) and that no such lands "shall, in any event, become liable to the satisfaction of any debt contracted prior to the issuing of the final patent in fee therefor" (Act of June 21, 1906, c. 3504, 34 Stat. 325, 327; 25 U.S.C. § 354, not quoted by petitioner but set forth in the note[6]). Yet federal income taxes are debts. *Price* v.

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[5] Petitioner discusses this latter statute in a footnote at p. 13 of his brief, dismissing it with the agreeable supposition that it merely made clear that Indian lands transferred in fee to the Indians would thereafter be subject to state and local taxation, federal direct taxation of lands being unknown in 1906 (when the statute was adopted) because of the apportionment requirement of the Constitution. Petitioner wholly overlooks that this statute speaks not merely of taxation, but equally of the more-inclusive term "incumbrance"—with respect to which the text above immediately proceeds. More important, petitioner misapprehends the policy or purpose of the provision of the allotment acts, as to which see the text, below. Congress had no purpose to insure that the states affirmatively *tax* Indians (which some state constitutions forbade; cf. United States *v.* Rickert, 188 U.S. 432, 441) but Congress was concerned with a policy of protection of the Indians until competency be established.

[6] The Indian Department Appropriation Act for 1907, Act of June 21, 1906, c. 3504, 34 Stat. 325, 327, provided in part:

> "That the Act entitled 'An Act to provide for the allotment of lands in severalty to Indians on the various reservations, and to extend the protection of the laws of the United States and the Territories over the Indians, and for other purposes,' approved February eighth, eighteen hundred and eighty-seven, be, and is hereby, amended by adding the following:
>
> "No lands acquired under the provisions of this Act shall, in any event, become liable to the satisfaction of any debt

United States, 269 U.S. 492, 499; *Massachusetts* v. *United States*, 333 U.S. 611, 625, and cases cited n. 24.

Finally, the statute says that when the restrictions are removed, then the allottee shall have the land (timber) "in fee, discharged of said trust and free of all charge or incumbrance whatsoever." 25 U.S.C. 348 (quoted in Petr. Brf. p. 41).

The ordinary content given the word "incumbrance" includes a diminution in value. *Miller* v. *Schwinn* (C.A.D.C., 1940), 113 F. 2d 748, 751; *Westerlund* v. *Black Bear Min. Co.* (C.A. 8, 1913), 203 Fed. 599, 605-6. When the United States sells the timber, the land, of the Indian ward and helps itself for "taxes" to the capital proceeds of land which it has never turned over in the first place there has, indeed, been "diminution in value." To that extent the title has been "incumbered."

Why has Congress adopted such a policy in the allotment acts; what purpose did Congress mean to achieve in the restrictions on sale, incumbrance, and taxation? This Court has said the purpose was "to prepare the Indians to take their place as independent, qualified members of the modern body politic" (*Board of Comrs.* v. *Seber*, 318 U.S. 705, 715); that the purpose of the law is to protect the Indian interest (*Sage* v. *Hampe*, 235 U.S. 99, 105); and that "The purpose of the restrictions was to give the needed protection, and they should be construed in keeping with that purpose" (*Smith* v. *McCullough*, 270 U.S. 456, 464-5). As to taxation, "while relating to the welfare of the Indians, the maintenance of the limitations which

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contracted prior to the issuing of the final patent in fee therefor.

"That no money accruing from any lease or sale of lands held in trust by the United States for any Indian shall become liable for the payment of any debt of, or claim against, such Indian contracted or arising during such trust period, or, in case of a minor, during his minority, except with the approval and consent of the Secretary of the Interior. * * *".

Congress has prescribed as a part of its plan of distribution is distinctly an interest of the United States." (*Heckman v. United States*, 224 U.S. 413, 437). "To lessen the difficulty of the period of transition and to protect the allottees' interest in their lands, Congress by the device of the trust patent or a restricted fee denied them the power to alienate or encumber their lands for fixed periods of time, subject to extension—denials which were sustained as proper exercises of Congressional power" (*Board of Comrs. v. Seber*, 318 U.S. 705, 715). Apparently petitioner would let you believe that the principle of the statute is merely a facet of the instrumentality doctrine. Petr. Brf. p. 15, quoting *United States* v. *Rickert*, 188 U.S. 432, 437. But this Court has found more even as to that decision: "But the decision [in the *Rickert* case] rested upon a broader foundation than the mere holding of a legal title to land in trust, and embraced the recognition of the interest of the United States in securing immunity to the Indians from taxation conflicting with the measures it had adopted for their protection." *Heckman* v. *United States*, 224 U.S. 413, 440-1.

Now if there shall control the purpose which this Court has repeatedly discerned, how would the tax here fit that Congressional purpose? Would respondent husband, who was to receive, when his competency is established, a patent in fee and thereupon get his inheritance, be better protected in assuring that he gets all of that inheritance intact than by permitting the United States to take under the guise of taxes a substantial part of that capital asset with which he would otherwise have been launched? Would the Congressional policy which strained at the gnat of the local real-estate tax readily swallow the cannonball of the federal income-tax, where both are paid at the expense of the very property?

To be borne in mind, too, is the legal status of these re-

strictions on encumbrance incorporated as they are not only in the statute but also in the so-called "patent".[7] For the right of exemption is a property right; it is protected by the Constitution. *Choate* v. *Trapp*, 224 U.S. 665, 673-4; *Carpenter* v. *Shaw*, 280 U.S. 363, 367.[8] The general rule refusing to presume tax exemptions and construing them strictly has no place in construing these statutes. *Carpenter* v. *Shaw*, 280 U.S. 363, 366; *Choate* v. *Trapp*, 224 U.S. 665, 675. The restrictions constitute "an express trust for a valuable consideration to the faithful performance of which the United States was legally committed." *United States*

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[7] This Court has characterized the "patent", as a term for what was issued here, as being inept, and some later cases have referred to it instead as a certificate of allotment. "The word 'patents,' where it is first used in this section, was not happily chosen to express the thought which, it is clear, all parts of the section being considered, Congress intended to express." United States v. Rickert, 188 U.S. 432, 436. "Congress . . . was careful to avoid investing the allottee with the title in the first instance, and directed that there should be issued to him what is inaptly termed a patent . . . but is in reality an allotment certificate. . . ." Monson v. Simonson, 231 U.S. 341, 345. This initial "trust patent", as it is frequently called (COHEN, *Handbook of Fed. Ind. Law*, p. 109), is entirely distinct from the fee patent which it promises.

[8] When we speak here of the right vested in the individual Indian respecting the status of his land as being beyond impairment or invasion in the sense of alienation encumbrance, taxation, etc., we do not overlook the cases holding that there is no such right vested in him as will defeat further action by Congress in discharge of its guardianship. Thus, the trust period in allotments may be extended, Tiger v. Western Investment Co., 221 U.S. 286, 309-316; Heckman v. United States, 224 U.S. 413, 428, and "until final patent be issued no vested right is obtained by the Indian which would support a constitutional objection to the enlargement of the period of the restriction." United States v. Jackson, 280 U.S. 183, 191. Likewise, the trust period may be reimposed on allotments theretofore freed of the trust. Brader v. James, 246 U.S. 88, 96. *Cf.* McCurdy v. United States, 246 U.S. 263, 273.

v. *Ferry County, Wash.* (E. D. Wash., 1938), 24 F. Supp. 399, 400. And indeed it is an express trust; both the statute (25 U.S.C. §348, quoted Petr. Brf. p. 41) and the patent itself (R. 14) declare "that the United States does and will hold the land thus allotted . . . in trust for the sole use and benefit of the . . . [allottee and his heirs] and that at the expiration of said period the United States will convey the same by patent to said Indian, or his heirs as aforesaid, in fee, discharged of said trust and free of all charge or incumbrance whatsoever." . . .

Whether the conversion of this undelivered birthright and its dissipation in income taxes is a relatively large or small portion of the whole should, we recognize, make no difference in principle; we do not argue legitimacy on the basis of the size of the baby. Still, the subversion of the Congressional policy becomes gross and glaring when we see the relationship of the value of the timber to the value of the land minus the timber. This Court was apparently startled at the fact in *Starr* v. *Campbell*, 208 U.S. 527, 534, that $15,000 of timber had been removed from an Indian allotment in Wisconsin—and that there remained cut-over land worth only $1,000, so that if the timber were not included in the restraint on alienation it "would be reduced to small consequence if it be confined to one-sixteenth of the value of the land." So in the present case. We are dealing with lands on the western slope of the Olympic Peninsula, where the only value of the land is its forest product.[9]

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[9] It was alleged in this case (R. 9) that the lands involved were heavily timbered, that the principal value was in the timber growing on them, and that the cost of reducing the lands to an arable condition fit for grazing or crop production is prohibitive—which allegations in the main are admitted in the answer (R. 31). It is notorious historical and ecologic fact in this area anyway:

> "Many operators thought they were not only making lumber but liberating the land from the trees, making room for

To the extent the United States fails to set up respondent husband with all his capital intact, and in this case the most important part of his capital, from which point he can go forward with a chance of economic survival in competition with others, to that extent the United States has violated its trust. Petitioner would have you understand that in some way the income-tax statutes scorned this trust—not by forthright repeal of the restrictions, but perhaps through some implication. But repeals by implication are not favored; and the intention of the legislature to repeal must be clear and manifest. *Rosenberg* v. *United States*, 346 U.S. 273, 294-5. A tax-exemption statute itself is subject to this limitation on repeal by mere implication.

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farmers. They advertised the cut-over areas for sale as farm land, and they found takers, for the price was low and the dream of a bit of land of one's own was almost universal. They were called stump ranchers, these hopeful people who came from everywhere to farm this new-won land. They grubbed at the great roots; they fought the encroaching salal and alder and huckleberry and the spikey, insinuating, indestructible blackberry vines. They raised a few crops and gave up, nearly all of them, though many wasted as much as a lifetime trying to grow truck and grain on land that, it finally became clear, was meant to grow only trees." MORGAN, *The Last Wilderness*, p. 131 (1955; Viking.)

"Similarly, ". . . professional foresters say that four out of five acres of forest land in western Oregon and Washington are fit to grow trees and nothing else. This fact did not become known suddenly, as if by revelation. It was recognized slowly, and only after more than half a century of attempts to prove otherwise . . . The unsuitability of the soil for crops was only one reason. What drove a majority of them from their hard-won acres was the appalling energy and power of the reviving forest: the second growth. . . . The forest's surge was so savage as to amaze a stump rancher over and over again, and so persistent as at last to discourage him. One day he reflected there *must* be an easier way to make a subsistence living, and he went away for good." HOLBROOK, *Far Corner*, pp. 239-240 (1952; Macmillan).

Posadas v. *National City Bank*, 296 U.S. 497, 503-6. How much more must it be true that there is no repeal by implication, that there is no repudiation of the Government's trust, when to construe the statute as implying such a repeal or repudiation would raise the serious constitutional question of a taking of the property right (*Choate* v. *Trapp*, 224 U.S. 665, 673-4; *Carpenter* v. *Shaw*, 280 U.S. 363, 367) of respondent husband without just compensation, contrary to the 5th Amendment.

Instead of repealing or watering down, Congress has affirmatively continued the trust period—it has recognized the necessity for continuance of the restrictions. 25 U.S.C. § 462 (quoted Petr. Brf. p. 45). So has the Executive annually to date as to reservations where that automatic statutory continuance of the trust did not apply. 25 C.F.R. c. 1, App.

Petitioner should not expect the courts to review and revise this Congressional policy. Long ago, this Court noted respecting the tax exemption of Indian lands (*United States* v. *Rickert*, 188 U.S. 432, 445):

> "It is said that the State has conferred upon these Indians the right of suffrage and other rights that ordinarily belong only to citizens, and that they ought therefore, to share the burdens of government like other people who enjoy such rights. These are considerations to be addressed to Congress. It is for the legislative branch of the Government to say when these Indians shall cease to be dependent and assume the responsibilities attaching to citizenship. That is a political question, which the courts may not determine. . . ."

Or (*Tiger* v. *Western Inv. Co.*, 221 U.S. 286, 315):

> ". . . it may be taken as the settled doctrine of this court that Congress, in pursuance of the long-established

> policy of the Government, has a right to determine for itself when the guardianship which has been maintained over the Indian shall cease. It is for that body, and not the courts, to determine when the true interests of the Indian require his release from such condition of tutelage."

And so we have a scheme for transplanting people of a vastly different culture into our own culture, contrived with the hope there would be as little economic shock as is possible; we have the deliberately-expressed purpose of Congress that such portion of the former communal lands as is marked out as an economic base for the individual be handed to him intact and without charge or diminution when he shall have completed his apprenticeship in individual ownership; we have the forthright assumption of a trust to accomplish that purpose assumed pursuant to Congressional direction, and with no repudiation of that trust by Congress. Yet petitioner would have you conclude that when the government sells the trust *res* which it has never yet delivered to the allottee, in some way the allottee has engaged in an income-producing enterprise so that the government itself is entitled to share substantially in the proceeds. We ask that you recognize that this not merely is an invasion of the trust but a subversion of the entire plan of the allotment acts, and merely masquerades as a tax.

II. The Allotment, as the Capital Stake to Be Given the Allottee When Found "Competent," Was Never "Acquired" by Him Before Sale of the Timber; and His Basis for Capital-gain Purposes Is Not Different from the Proceeds of the Timber.

Petitioner says respondents were properly taxed because they enjoyed a "gain." 1939 I.R.C. § 112(a). If

they had a gain, it is because they realized upon sale of their timber an excess over its adjusted basis. *Id.*, § 111(a). Its basis was either its cost or, if it were "acquired" prior to March 1, 1913, alternatively its March 1, 1913, fair market value. *Id.*, § 113(a)(14). Regardless of when "acquired", certain adjustments must be made to derive the adjusted basis. Id., § 113(b). In this case, from the proceeds of sale of the timber there was deducted the 1913 value of the timber on the allotment. R. 20.

Another and significant part of petitioner's argument is founded on a misconception of the record—all too reasonable a misconception, we must acknowledge, though one which the respective counsel who prepared the case for trial could scarcely have felt likely.[10] Petitioner states over and over that respondents' income arises from "the cutting and sale of timber." Now that is logging, an ordinary commercial enterprise; and petitioner's reading of the record that that is the business in which respondent husband was engaged strongly flavors the argument.

Actually, all respondent husband had to do with this "cutting and sale" was to consent to the deal made by the government representative for the sale of the timber standing on his allotment. See § 61.13 of the "General Forest Regulations", 25 C.F.R. (quoted in Petr. Brf. p. 48). See the Complaint, § VII, R. 6-7; the Answer, § 7, R. 30-31; the stipulation, § VIII, R. 36. The trial judge found from this (R. 39) that in 1943 timber was cut, sold and paid for from respondent husband's land pursuant to a contract of sale by the Bureau of Indian Affairs "providing for the cutting and sale of timber from plaintiffs'

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[10] Counsel for respondents in the trial court was Kenneth R. L. Simmons, Esq., of the Montana bar, who died not long after preparing the brief in the Court of Appeals for the Ninth Circuit.

said lands".[11] To conclude from this that respondent husband, an incompetent reservation Indian, was engaged in "the cutting and sale of timber . . . an ordinary income-producing operation" (Petr. Brf. p. 17, 18, 19, 20), in the circumstances is highly incongruous.

The fact is that respondent husband, up to any time here material, never did "acquire" this land so as to have a basis for gain or loss. Never yet had he received his capital upon which he might thereafter make a gain. To

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[11] We are asking for a statement from the Bureau of Indian Affairs as to the precise manner in which this sale was conducted. We hope this will be in our hands prior to the argument and may be considered by the Court so that the distortion imported into this record for want of familiarity with the local pattern and because of the inadequately-expressed assumptions on the basis of which this case was pleaded may not mislead the Court as to the facts.

The pattern of these sales on the Quinaielt Reservation has recently been the subject of a Congressional investigation at Aberdeen, Wash., November 28, 1955 (Joint Hearing of Sub-committee on Legislative Oversight Function of the Senate Committee on Interior and Insular Affairs, and of the Sub-committee on Public Works and Natural Resources of the House Committee on Government Operations). We understand that those hearings are to be printed, though as this is written they are unavailable. The hearings disclosed the usual pattern to include the setting up from time to time of a large "cutting unit" of from hundreds to 30,000 and more acres, all covered under one contract of the government, but applicable to any given allotment only as the allottee (or, if it be "heirship status", a majority interest of the heirs) may theretofore have consented through having signed a power of attorney to the superintendent presented by the agency officials. The way these sales have been conducted was there shown to bring scandalously low prices, due to a variety of reasons including the monstrous size of the "units" so that there could be little or no competition; and a requirement that by instalments in the first three years there be paid half of the value (according to an old cruise) of the standing timber (the balance being payable as the logger cuts out the unit). As a result of this latter requirement, an immediate investment of hundreds of thousands of dollars might be required, even though the unit might take over 30 years to cut out. Certainly the ordinary

be sure, the Congressional scheme in the allotment acts discloses a purpose that the Indian shall, until his competency be established, have the use of that land. And we may, for present purposes, assume that the crops he might raise or the rentals he might receive from its current exploitation would be taxable. (We cited the cases, both ways, on this proposition in notes 2 and 3, p. 7, above.) But that use of the land does not extend to the sale of the standing timber, which is part of the land itself,

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restricted Indian on this reservation is not engaged in "the cutting and sale of timber . . . an ordinary income-producing operation" (Petr. Brf. p. 17, 18, 19, 20).

Another distortion (although we can scarcely criticize present counsel in the circumstances) arises from counsel's reading of the General Timber Sale Regulations with respect to "sustained yield" of the forest. Petr. Brf. 23-4. As was demonstrated in the Aberdeen hearing, "sustained yield" on the Olympic Peninsula and specifically on the Quinaielt Reservation, does not mean what it may mean elsewhere. In that area, opening up the forest by selecting only a part of the merchantable timber at any particular place usually results in windthrow of the entire balance. And any notion that "sustained yield" could be practiced on the relatively trifling area of a single allotment (in this case, 93.25 acres, R. 13) is bizarre. What the regulations are addressed to, and the substantial area in which they operate, is on the large forests of *tribal* timber, standing on tribally-owned lands on many reservations—*e.g.*, the Menominee Reservation in Wisconsin. For petitioner happily to conclude that "the only conclusion possible is that the value of the taxpayers' trust property was not diminished by the sale of the original standing timber; instead, it almost certainly was increased" (Petr. Brf. p. 21) is fantastic. We would think it a matter of common knowledge, of which this Court would take notice, that timberland is worth less after it is cut (whether selectively or not) than it was before, and that its price is depressed in direct proportion to the value of the stumpage removed. We would think, too, that of all places in the world where the value of the land would be overwhelmingly reduced by cutting the timber the most outstanding would be this virgin forest on the western slope of the Olympics. Cf. HOLBROOK, *Far*

United States v. Cook, 19 Wall. 591, 593. The statute and the "trust patent" both have promised that the land itself (not just part of it or part of its value) shall be turned over to him when competency is established "in fee, discharged of said trust and free of all charge or incumbrance *whatsoever*"—which plain English must mean without the trustee's taking a chunk of the *res* for its own. He must, then, look to the future for his capital; only after he receives it can he deal in it and have "gains".[12]

Corner (1952, Macmillan), pp. 239, 241-2. One of the judges (Bone, J.), familiar with the area, remarked at the argument below that it would take "hundreds of years" to replace the forest cut from the allotment.

We covered under the first heading in our argument (pp. 13, 14, n. 9, above) the proposition that the only substantial value of the allotment was in its forest.

Should there be a disposition on the part of the Court to have the case turn on these considerations now advanced by petitioner, (a) whether respondent husband engaged in the business of "cutting and sale of timber," that is, obtained the proceeds in question by engaging in the logging business; or (b) the value of the allotment before and after cutting of the timber; or (c) the "selective logging" practiced in pursuit of a "sustained-yield" program for the allotment, then we respectfully request that the Court remand the case to the district court for taking evidence on those facts.

[12] Thus, out of some $15,080.80 timber sold from this allotment, and out of the $8,418.28 paid for during the taxable year, only $1,537 was disbursed to respondents during that year. To the extent, then, of $1,537 respondent husband had had delivered to him his share of the aboriginal communal lands—that is, the proceeds of conversion of the timber. If he invest that (or if the government, *qua* trustee, invest for him the remaining proceeds), as by purchasing timber land and selling stumpage at a profit, we may concede it would be taxable, since not within the Congressional policy. This Court has so held with respect to income from invested funds the source of which had been an allotment. Superintendent Five Civ. Tr. *v.* Commissioner Int. Rev., 295 U.S. 418, 421. We believe that that would extend to capital-gains income as well as to ordinary interest and dividends. But the tax problem in such a situation, where the allottee has received his capital, is

Until the property is conveyed to respondent husband free of trust he has no more "acquired" it than the optionee "acquired" for capital-gain purposes the real property involved in *Helvering v. San Joaquin Fruit & Inv. Co.*, 297 U.S. 496, 498-9:

> ". . . The option itself was property, and doubtless was valuable. If it had been assignable, and the lessee had sold it at a profit, taxable gain would have resulted from the sale. But the option is admittedly not the same property as the land. . . . even if we should agree that a lessee-optionee acquires, by virtue of the instrument, an equitable interest in the land it would not follow that, within the contemplation of the revenue acts, he acquires the property at the date of the option rather than at the date of conveyance. . . . In the common and usual meaning of the term the land was acquired when conveyed to the respondent's predecessor."

Cf. *McFeely v. Commissioner*, 296 U.S. 102, 107.

Petitioner indicates that the "removal of timber constitutes in part a wasting of the capital asset" so that the tax laws contain provisions to exclude from tax "such portion of the proceeds of the sale of timber as represents such waste." (Petr. Brf. p. 17.) Reliance is placed on an alternative provision of the tax law under which taxpayers may recoup their basis in timber through depletion deductions. No doubt, once respondent husband were to receive his capital in the form of standing timber (impossible in this particular case), and so acquire the timber as a capital asset, he would be in economic position to elect the depletion

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very different from the situation where the government's trust to carry the portion of the ancient tribal lands into the tribal members' hands individually without charge or incumbrance had never yet been carried out.

method if it were advantageous. 1939 Code § 114(b). Even were the courts below wrong and respondents taxable on these proceeds, that would make no conceivable sense here; better they should elect the capital-gains treatment. *Id.*, § 117(k)(2). But the point is a mere distraction in the light of the essential fact here that thus far respondent husband has not received the capital asset to deplete. And it borders on the inane to say on these facts, where all respondents did was to assent to the sale by the government, that what was received for the timber was only "in part" the value of that asset. It is all respondents got or ever will get for that asset. No part of it represented their own labor or enterprise; there was simple substitution of the cash asset for the timber, both held by the government.

This point is urged because our opposition to the petition asserted that *Jones* v. *Tannah* (C.A. 10th, 1951), 186 F. 2d 445, cert. den. 341 U.S. 904, was distinguishable as involving oil royalties from a restricted allotment—the annual payment of which represented restoration of the basic capital itself (under the liberal oil-depletion provisions) and the other part the annual product of the land. This Court itself had pointed out that "The depletion effected by production is likened to the depreciation of machinery or the using up of raw materials in manufacturing. . . . The deduction is therefore permitted . . . as compensation for the capital assets consumed in the production of income through the severance of the minerals." *Anderson* v. *Helvering*, 310 U.S. 404, 407-8. (See, also, *Helvering* v. *Elbe Oil Land Co.*, 303 U.S. 372, 375; *Badger Oil Co.* v. *Commissioner Int. Rev.*, C.A. 5th, 1941, 118 F. 2d 791, 793.) But it is no answer in this case that respondents might have elected a useless depletion deduction, for (a) they were not engaged in the annual cutting and sale of timber; they were not in the logging business at all; (b) that deduction is not, in the case of timber, even roughly designed

to accord the Indian the unincumbered value of his allotted land, since it would not return the current value, but only the March 1, 1913, value; and nothing less than the full capital value of the land (timber) could substitute for getting that land "free of all charge or incumbrance whatsoever"; (c) finally, this was treated as sale of a capital asset, and we know of no reason why the election would not be conclusive on petitioner.

Though respondent, as a result of the tax, has neither the unincumbered land which Congress has promised him out of the ancestral holdings nor the undiminished proceeds, petitioner rings the changes on the doctrine stemming from *Willcuts* v. *Bunn*, 282 U.S. 216, 227-228, that a tax on profits arising from sale of property is not a tax on the property itself. Thus, in *United States Trust Co.* v. *Helvering*, 307 U.S. 57, 60, it was held that an estate tax is not a tax upon the property of which the estate was composed but an excise upon the transfer or shifting in relationships of property at death. Does that apply to allotted lands still under trust as are those of respondents? A reading of petitioner's brief (pp. 25-29) seems to say so, over and over again, relying on *Oklahoma Tax Comm.* v. *United States*, 319 U.S. 598.

That case held precisely the contrary of what petitioner asserts; petitioner happily relies only on so much as relates to the non-restricted-land property involved (p. 600). Here is what this Court held with respect to so much as is material here (pp. 610-11):

> "The validity of the taxes on the transfer of the land presents a somewhat different problem. Some of these lands are exempt from direct taxation by virtue of explicit congressional command. The Act of May 10, 1928, 45 Stat. 495, for example, provides that Indians of a class which includes the three deceased should

> select up to 160 acres of his allotted, inherited or devised restricted lands, which 'shall remain exempt from taxation while the title remains in the Indian designated . . . or in any fullblood Indian heir or devisee,' while all other restricted lands are made subject to taxation by Oklahoma. The State argues that congressional exemption of the land from direct state taxation does not exempt the land from an estate tax, because of the principles announced in *United States Trust Co.* v. *Helvering*, *supra*. A majority of the Court concludes that this principle does not apply to Indian lands specifically exempted from direct taxation. We therefore hold that the transfer of those lands which Congress has exempted from direct taxation by the State are also exempted from estate taxes."

That holding disposes of petitioner's citations of *Graves* v. *N. Y. ex rel. O'Keefe*, 306 U.S. 466, and *O'Malley* v. *Woodrough*, 307 U.S. 277, since those cases were specifically discussed and the ruling we have quoted was therefore formulated with those cases in mind. The two later *Oklahoma Tax Comm.* cases relied on by petitioner involve, respectively, property other than restricted or tax-exempt lands (*West* v. *Oklahoma Tax Comm.*, 334 U.S. 717), and a tax not on the Indians at all but one against lessees under oil-and-gas leases of restricted Indian land, the tax being an excise on the production of oil by the lessees—the Court noting (p. 353) that "There is no possibility that ultimate liability for the taxes may fall upon the [Indian] owner of the land" (*Oklahoma Tax Comm.* v. *Texas Co.*, 336 U.S. 342).

Repeatedly petitioner relies on one particular case, pointing out that it was cited "with approval" in the case of *Oklahoma Tax Comm.* v. *United States*, 319 U.S. 598, which latter case, as demonstrated by the quotation above, peti-

tioner has misread. That case is *Landman v. Commissioner Int. Rev.* (C.A. 10th, 1941), 123 F. 2d 787, cert. den. 315 U.S. 810. Its use without more compounds the misleading quality of this portion of petitioner's argument. For the holding of that case that an estate tax is merely an "excise tax upon the shifting of the economic burdens and benefits, or on the privilege of transferring property of decedent at death" (123 F. 2d at p. 790) was directly read from *United States Tr. Co. v. Helvering*, 307 U.S. 57, which this Court specifically held, as we have quoted, does not apply to restricted Indian lands. And why petitioner would cite to you only the one *Landman* case, while there are two later *Landman* cases which clearly dissipate this argument petitioner builds on the older one, is perplexing:

(1) *Landman v. United States* (1945), 103 C. Cls. 199; 58 F. Supp. 836, following not long after the 319 U.S. *Oklahoma Tax Comm.* case, specifically held that a restricted allotment itself is not subject to federal estate tax, the Court of Claims quoting (103 C. Cls. at p. 209) not only this Court's majority opinion, but the minority opinion to the same effect (319 U.S. at p. 614, n. 2). Possibly because the Court of Claims reading of this Court's determination was so plainly correct certiorari was not applied for.

(2) *Landman v. United States* (1947), 109 C. Cls. 1, 71 F. Supp. 640, cert. den. 332 U.S. 815, held again that restricted allotted land was not includable in gross estate for the sake of the federal estate-tax laws, but held that oil and gas royalties, reinvested in bonds, livestock, and real estate, was subject to the tax—a flat agreement with the decision of this Court as to the state taxes involved in the 319 U.S. *Oklahoma Tax Comm.* case, and in accord, it later developed, with this Court's holding as to state taxes in the 334 *U.S. Oklahoma Tax Comm.* case. And the Court of Claims specifically noted that the rationale of the first

Landman case (C.A. 10—the one cited by petitioner) "seems to us to be in conflict with what we conclude, as above shown, to be the rationale of the decision in *Oklahoma Tax Commission v. United States*, *supra*, [319 U.S. 598], holding that the allotted lands there involved were immune from the Oklahoma estate tax."

Petitioner's remaining answer is that "these Indians are not entitled to any better treatment than is accorded to other taxpayers who own timber lands and who are taxed with income as it is realized." (Petr. Brf. pp. 20-21, n. 7.) This bespeaks a subtle prejudice we urgently wish to point up.

Of course Indians are not entitled to "better treatment" than other taxpayers. But that there may be special Congressional policy with respect to some of them is no more remarkable than that there may be some special policy with respect to labor organizations or farmers or mutual insurance companies. And where one of the more fortunate Indians, "competent" or not, engages in the ordinary acquisition of timber lands and the cutting and sale of forest products, he is in every respect on the same basis as his non-Indian neighbor. There are thousands of Indians who are "competent"; who have received their lands in fee (and may have sold or lost them), and who pay federal income taxes exactly as do any non-Indians.

But there are also thousands of tribal Indians in this country who present a special problem, a problem not readily solved. It is common experience that nearly any uninformed person will hold forth readily as to the solution of the "Indian problem"—which solution usually consists of the assertedly-simple expedient of putting Indians on just the same basis as "everyone else". There is never a thought to deeply established cultural barriers which cannot be abolished by legislative fiat or court decision, including cultural values just as stubbornly held by most

Indian communities as by our own. There is never a thought to the tribal government as a government, with its own laws and ways of adjudging conflicts, and self assurance of its virtues frequently equal to our own. There is never a thought to tribal property, and the variety of communal existence which makes the "Indian problem" not a single problem but a whole gamut.

May the solution be reached merely on the basis of the offhand, uninformed and prejudiced view which petitioner advances in this statement? May this Court—with or without its own notions as to solutions—attempt to fashion some portion of remedy on those limited occasions when some case touching the Indians comes before it? Or is not Congress the keeper of the national conscience[13] must there not be applied to *these* Indians—non-competent, full-blood, reservation Indians—the policy and purpose in dealing with the problem which Congress has provided?

And does application to these Indians of valid federal law designed for the very purpose of carrying out the Congressional policy accord them "any better treatment than is accorded to other taxpayers"?

Conclusion

The judgment below should be affirmed.

Respectfully submitted,

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[13] *Cf. United States v. Realty Co.*, 163 U.S. 427; *Pope v. United States*, 323 U.S. 1, 9-10.